

REDACTED -- FOR PUBLIC INSPECTION

June 26, 2000

Ms. Royce Dickens
Deputy Chief, Policy and Rules Division
Cable Services Bureau
Federal Communication Commission
445 12th Street, S.W. The Portals
Washington, D.C. 20554

Re: Response to June 9, 2000 Request for Further Information In the Matter of Applications of America Online, Inc. and Time Warner Inc. for Transfers of Control, CS Docket No. 00-30

Dear Ms. Dickens:

This letter sets forth the narrative responses of America Online, Inc. (AOL) and Time Warner Inc. (Time Warner) to the June 9, 2000 letter from Ms. To-Quyen Truong, Associate Chief of the Cable Services Bureau, requesting certain documents and information (the Information Request). In accordance with the Information Request and the Protective Order adopted by the Cable Services Bureau on April 6, 2000,¹ the parties are filing the documents which accompany these narrative responses under separate cover letter.

* * *

AOL s Ownership Interest in Hughes Electronics Corporation (Hughes)

The Commission s Information Request begins with a series of questions concerning AOL s indirect interest in Hughes, which controls direct broadcast satellite (DBS) provider DirecTV. Before responding to the specific questions asked by the Commission concerning AOL s investment in Hughes, we set forth below a brief overview of this investment and the nature of AOL s interest.

In pursuit of its previously described multiple platform distribution strategy of AOL Anywhere, AOL last year announced a strategic alliance with Hughes to develop and market Internet services nationwide via satellite. As part of that agreement, AOL made an investment in General Motors Corporation, the parent company of Hughes, to accelerate the development of DBS as a platform for the next generation of Internet services. That investment was not intended to, and

¹ *In the Matter of Applications of America Online, Inc. and Time Warner Inc. for Transfers of Control*, CS Docket No. 00-30, Order Adopting Protective Order, DA 00-780 (CSB April 6, 2000).

does not, provide any opportunity for AOL or the merged AOL Time Warner to participate in DirecTV's video programming operations.

As detailed below, AOL's interest in General Motors takes the form of a non-convertible stock which, even upon conversion, would remain non-attributable under any set of rules applied in the cable context. Specifically, AOL's investment is currently in the form of a preference stock which provides no voting rights except in the extremely limited circumstances detailed below. Even after conversion to a GM common stock that tracks the economic performance of Hughes, AOL's interest would still be non-attributable under any even potentially relevant FCC attribution rule. In particular, upon conversion, AOL's voting interest in General Motors would be significantly below the five percent threshold for attribution under the Commission's cable horizontal ownership provision.²

In June 1999, AOL invested \$1.5 billion in General Motors Corporation in return for shares of GM's Series H 6.25 percent Automatically Convertible Preference Stock (the Series H Preference Stock).³ AOL holds all of the outstanding shares of the Series H Preference Stock.⁴ These non-attributable shares do not entitle AOL to voting rights, except in the most limited situations.⁵ These shares will automatically convert into shares of GMH stock on June 24, 2002, unless the shares have been converted earlier.⁶

² See 47 C.F.R. § 76.503.

³ See Excerpts from General Motors Corporation Offer to Exchange 1.065 Shares of Class H Common Stock for each share of \$1 2/3 Par Value Common Stock, at 117 (Exchange Offer). The complete document is available at <http://www.gm.com/company/investors/stockholders/class_main.html>.

⁴ *Id.*

⁵ AOL is entitled to vote on amendments or alterations to any provision of the GM Restated Certificate of Incorporation or the Certificate of Designations of Series H 6.25% Automatically Convertible Preference Stock of General Motors Corporation which would adversely affect the powers, preferences or special rights of the Series H Preference Stock. Exchange Offer at 120; Certificate of Designations of Series H 6.25% Automatically Convertible Preference Stock of General Motors Corporation, at Section 5(ii) (Certificate of Designations). Further, in the event that (1) GM fails to pay, in full, the preferential dividends accumulated on AOL's Series H Preference Stock for any six quarterly dividend payment periods (whether or not consecutive), and (2) all such dividends remain unpaid, the number of directors of GM will be increased by two and AOL will elect such directors. *Id.* If holders of other series of preference stock are entitled to vote on the election of such directors due to a preferential dividend default with respect to those series, AOL, as the sole shareholder of Series H Preference Stock, and the holders of these other series of preference stock will elect such directors together as a class. *Id.*

⁶ *Id.*

GM's GMH stock is a tracking stock designed to provide holders with financial returns based on the financial performance of Hughes.⁷ The outstanding GMH shares, however, do not represent the full interest in Hughes. Rather, GM has retained part of that value for itself. GMH stockholders are common stockholders of General Motors and, as a result, have rights in the equity and assets of GM rather than of Hughes.⁸ GM's Certificate of Incorporation entitles holders of both GM and GMH stock to a fixed number of votes per share on all matters submitted to GM's common stockholders for a vote.⁹ GMH stock votes separately as a class only on any amendment to the GM Certificate of Incorporation which adversely affects the rights, powers or privileges of the GMH stock or increases the number of authorized shares of GMH stock.¹⁰

Recently, GM has made three announcements affecting the GMH stock. First, on February 2, 2000, it announced a plan to repurchase up to 14 percent of its outstanding GM common stock in exchange for shares of GMH stock.¹¹ Under that offer, GM proposed to issue 1.065 shares of GMH stock for each share of GM common stock tendered pursuant to the offer, up to a maximum of 86,396,977 GM shares.¹² On May 26, 2000, GM announced that it had accepted 86,396,977 shares of GM stock in exchange for a total of 92,012,781 shares of GMH stock.¹³ Second, on June 6, 2000, GM declared a three-for-one stock split of the GMH stock. The stock split will be in the form of a 200 percent stock dividend, payable on June 30, 2000, to GMH stockholders of record on June

⁷ Exchange Offer at 124.

⁸ *Id.* at 29. Although the net income of Hughes is allocated for accounting purposes to calculate the amounts which may be used to pay dividends on each class of GM common stock, this allocation does not result in a physical segregation of the assets of GM or Hughes, or the establishment of separate accounts or dividend or liquidation preferences. *Id.* at 29, 124. If a liquidation, insolvency or similar event occurred with respect to Hughes, creditors of Hughes, as well as GM as the sole stockholder of Hughes, would receive payment from the assets of Hughes. *Id.* at 29. The holders of GMH stock would not be entitled to any payment from the assets of Hughes. *Id.* at 29.

⁹ Exchange Offer at 129; General Motors Corporation Restated Certificate of Incorporation, As Amended June 24, 1999, at Article 4, Division I(b) (Certificate of Incorporation).

¹⁰ *Id.*

¹¹ General Motors Corporation, Current Report, SEC Form 8-K, February 2, 2000.

¹² *Id.*

¹³ GM Announces Final Results of Successful Exchange Offer, May 26, 2000.

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13, 2000.¹⁴ Third, on June 13, 2000, GM announced that it had contributed 60,500,000 shares of GMH stock to certain of its employee-benefit plans on June 12, 2000.¹⁵

With this background regarding the AOL interest, we respond to the Commission's specific inquiries below.

1.1 At page 11 note 15 of the Supplemental Information (SI) statement, Applicants state that AOL invested \$1.5 billion in a General Motors (GM) equity security and that GM then invested the \$1.5 billion in a security of Hughes under similar terms. The SI further states that GM has a current market capitalization (at the date the SI was filed) in excess of \$50 billion.

a. What is General Motors' current market capitalization?

GM currently has outstanding several classes of shares, including the GM common stock and GMH stock discussed above. As of June 22, 2000, the price per share of each of those classes of stock, as well as the total value of outstanding shares, was as follows:¹⁶

¹⁴ GM Announces Three-For-One Split of Class H Stock, June 6, 2000.

¹⁵ GM Announces \$5.6 Billion Contribution to Employee-Benefit Plans, June 13, 2000.

¹⁶ GM Stock Quotes, <<http://www.nyse.com/>> (visited on June 22, 2000).

SYMBOL	NUMBER OF SHARES OUTSTANDING	PRICE PER SHARE	TOTAL VALUE OF OUTSTANDING SHARES
GM	537,784,403 ¹⁷	60	32,087,064,180.00
GMH	290,950,014 ¹⁸	103	29,967,851,442.00
GMPRD	3,015,000	25 1/16	75,563,437.50
GMPRG	5,015,000	26 1/8	131,016,875.00
GMPRX	3,150,000	24 15/16	78,553,125.00
GMPRY	5,221,000	26 3/8	137,703,875.00

Based on the foregoing, the total value of the outstanding shares of the various classes of General Motors stock as of June 22, 2000 was \$62,477,752,934.50.¹⁹

¹⁷ Because of recent changes in the GM and GMH capital structure, our calculations are based on information reported in the General Motors Quarterly Report for the first quarter of 2000, adjusted to reflect the publicly available information regarding the recent Exchange Offer and contribution to certain employee-benefit plans. General Motors Quarterly Report for the Quarterly Period Ending March 31, 2000, SEC Form 10-Q, at 1. The number of GM shares outstanding on March 31, 2000 was 621,181,380. *Id.* General Motors repurchased 86,396,977 shares of GM stock through the Exchange Offer. GM Announces Final Results of Successful Exchange Offer, May 26, 2000. The number of GM shares outstanding has been calculated by subtracting the number of shares repurchased through the Exchange Offer from the number of shares outstanding on March 31, 2000. $621,181,380 - 86,396,977 = 534,784,403$.

¹⁸ As noted, because of recent changes in the GM and GMH capital structure, our calculations are based on information reported in the General Motors Quarterly Report for the first quarter of 2000, adjusted to reflect the publicly available information regarding the recent Exchange Offer and contribution to certain employee-benefit plans. General Motors Quarterly Report for the Quarterly Period Ending March 31, 2000, SEC Form 10-Q, at 1. The number of GMH shares outstanding on March 31, 2000 was 138,437,233. *Id.* General Motors recently issued 92,012,781 shares of GMH stock as a result of the Exchange Offer. *See* GM Announces Final Results of Successful Exchange Offer, May 26, 2000. GM also contributed 60,500,000 shares of GMH stock to certain employee-benefit plans on June 12, 2000. GM Announces \$5.6 Billion Contribution to Employee-Benefit Plans, June 13, 2000. The number of GMH shares outstanding has been calculated by adding the number of GMH shares issued as a result of the Exchange Offer and the contribution to the number of GMH shares outstanding on March 31, 2000. $92,012,781 + 60,500,000 + 138,437,233 = 290,950,014$.

¹⁹ Prior to the Exchange Offer and contribution, the total value of the outstanding shares of GM stock was \$51,441,583,031.25, and the total value of the outstanding shares of GMH stock

b. What is Hughes current market capitalization?

As noted above, Hughes is a wholly-owned subsidiary of GM. Other than the GMH stock, which tracks a portion of the economic value of Hughes, Hughes has no outstanding public stock on which to base a market capitalization. However, as of June 22, 2000, the value of the outstanding GMH stock was \$29,967,851,442.00.

c. Please produce documents to support your answers to the questions in a. and b.

As noted above, the parties are providing documents in response to this request under separate cover letter.

1.2 At page 13 note 21 of your SI, Applicants state that AOL has 2,669,633 shares of GM s Series H 6.25% Automatically Convertible Preference Stock (Preference Stock). You state that this Preference Stock is convertible to GM s Class H common (GMH) stock, which is a publicly held tracking stock that tracks the economic value of Hughes.

a. Under what circumstances may AOL choose to convert its Preference Stock?

AOL may convert all or any portion of its preference stock at any time prior to the occurrence of a Tax Event or the Mandatory Conversion Date (June 24, 2002).²⁰ Upon the

was \$17,235,435,508.50. The total value of the outstanding shares of GM stock was calculated using the number of shares outstanding on March 31, 2000 (621,181,380) and the stock price of GM stock on that date (82 13/16). See General Motors Quarterly Report for the Quarterly Period Ending March 31, 2000, SEC Form 10-Q, at 1. The price of the GM stock on March 31, 2000 can be found at http://www.bigcharts.com/historical/default.asp?detect=1&symbol=gm&close_date=03%2F31%2F00&x=8&y=16. Likewise, the total value of the outstanding shares of GMH stock was calculated using the number of shares outstanding on March 31, 2000 (138,437,233) and the stock price of GMH stock on that date (124 1/2). See General Motors Quarterly Report for the Quarterly Period Ending March 31, 2000, SEC Form 10-Q, at 1. The price of GMH stock on March 31, 2000 can be found at http://www.bigcharts.com/historical/default.asp?detect=1&symbol=gmh&close_date=03%2F31%2F00&x=31&y=30.

²⁰ Certificate of Designations at Section 6(ii). A Tax Event is defined as any amendment to or change (including an announcement of a prospective change, such as but not limited to, the reporting of legislation by the House Ways and Means Committee or the Senate Finance Committee, or the proposal of a legislative change that has an effective date that is proposed to precede the date of enactment) in, the laws or regulations of the United States or any political subdivision or taxing authority thereof or therein, or any official administrative pronouncement or judicial decision interpreting or applying such laws or regulations, as a result of the enactment, adoption or issuance of which there is in the opinion of the Corporation s outside counsel more than an insubstantial risk that the Corporation or any subsidiary thereof is or will be subject to

occurrence of a Tax Event, GM or Hughes has the right to redeem or acquire all (but not less than all) outstanding shares of Series H Preference Stock. GM or Hughes must take such action on or before a Mandatory Redemption Date, and must give AOL advance written notice.²¹

b. If AOL were to convert its Preference Stock today, how many shares of GMH stock would it have?

AOL has 2,669,633 shares of Preference Stock which would be converted to GMH stock at an Optional Conversion Rate of 8.0645 shares of GMH stock for each share of Preference Stock.²² Thus, upon conversion, AOL would have 21,529,255 shares of GMH stock.²³

c. What percentage of GMH stock would AOL's GMH shares constitute?

As noted above, the outstanding shares of GMH stock do not represent a value based on the full financial performance of Hughes. Rather, the 290,950,014 shares of GMH stock presently outstanding track approximately 67.7 percent of the financial performance of Hughes.²⁴

If AOL were to convert its Series H Preference Stock, the number of outstanding shares of GMH stock would increase to 312,479,269.²⁵ AOL's GMH shares would represent 6.9 percent of the outstanding shares of GMH stock.²⁶ However, because all of the outstanding shares of GMH

more than an insignificant amount of Income Taxes with respect to the Series H Preference Shares, the shares of Class H Common Stock issuable upon conversion, exchange or redemption thereof, or any capital stock of the Corporation or any subsidiary issuable pursuant to [the Certificate of Designations of Series H 6.25% Automatically Convertible Preference Stock of General Motors Corporation]. *Id.* at Section 13.

²¹ *Id.* at Section 7.

²² Exchange Offer at 119; Certificate of Designations at Section 6(ii).

²³ Exchange Offer at 119.

²⁴ 290,950,014 (the number of GMH shares outstanding) divided by 431,500,000 (the denominator of the Class H fraction for the first quarter of 2000) equals 0.677 or 67.7 percent. *See infra* at Section 1.2(e).

²⁵ The sum of 290,950,014 (the number of GMH shares outstanding) and 21,529,255 (the number of GMH shares that AOL would receive upon conversion of its Series H Preference Stock) is 312,479,269.

²⁶ 21,529,255 (the number of GMH shares that AOL would receive upon conversion) divided by 312,479,269 (the total number of GMH shares that would be outstanding upon AOL's conversion of its Series H Preference Stock) equals 0.069 or 6.9 percent.

stock would represent only 69.0 percent of the total economic value of Hughes²⁷, AOL's GMH shares would represent shares tracking approximately 4.8 percent of the financial performance of Hughes.²⁸

d. What percentage of Hughes' economic value does AOL's Preference Stock represent?

As discussed above, AOL's shares of Series H Preference Stock are shares of General Motors stock. Although AOL may convert its shares of Series H Preference Stock into shares of GMH stock,²⁹ until AOL's Preference Stock is converted, AOL holds no direct or indirect interest in the financial performance of Hughes.

e. What percentage of Hughes' economic value would AOL's GMH stock represent?

As discussed above, GMH stock is a tracking stock designed to provide holders with financial returns based on the financial performance of Hughes. However, GMH stockholders would have no direct claim against the assets of Hughes because GMH stock is a common stock of GM and, in the event of GM liquidation, insolvency or a similar event, GMH stockholders would only have rights in the assets of GM as common stockholders of GM.

With respect to the economic performance of Hughes relative to the GMH stock, the GM Certificate of Incorporation allocates Hughes' earnings between the GM common stock and GMH stock based on a fraction referred to as the Class H fraction.³⁰ The Class H fraction reflects the tracking stock interests of each of GM's classes of common stock in the earnings of Hughes for dividend purposes.³¹

²⁷ 312,479,269 (the number of GMH shares that would be outstanding upon AOL's conversion of its Series H Preference Stock) divided by 453,029,255 (the denominator of the Class H fraction for the first quarter of 2000 adjusted to reflect the number of GMH shares that AOL will receive upon conversion of its Series H Preference Stock) equals 0.690 or 69.0%.

²⁸ The product of 0.069 and 0.690 by the GMH stock after the is 0.048 or 4.8%.

²⁹ See *infra* at 1.2(e) (discussing the characteristics of GMH stock, and the percentage of Hughes' economic value that AOL's GMH stock would represent).

³⁰ Exchange Offer, at 11, 126-27; Certificate of Incorporation, at Article 4, Division I(a)(4).

³¹ Exchange Offer, at 126.

Class H Fraction =
$$\frac{\text{Weighted Average Number of Shares of GMH Stock Outstanding During Any Applicable Accounting Period}}{\text{Weighted Average Number of Shares of Class H Common Stock During Any Applicable Accounting Period Which, If Issued and Outstanding, Would Represent 100 percent of the Tracking Stock Interest in the Earnings of Hughes}}$$

As of March 31, 2000, the numerator of the Class H fraction was 137,800,000 and the denominator was 431,500,000.³² Thus prior to GM's recent Exchange Offer and contribution to certain employee-benefit plans, the Class H fraction for the first quarter of 2000 was 31.9 percent. The GMH stock represented 31.9 percent of the economic value of Hughes on March 31, 2000. Today, with the additional GMH shares issued as a result of the Exchange Offer and contribution taken into consideration, the GMH stock represents approximately 67.7 percent of the economic value of Hughes.³³

Upon conversion of the Preference Stock into GMH stock, both the numerator and denominator of the Class H Fraction will increase by the amount of GM Class H stock issued.³⁴ As noted above, we estimate that the AOL GMH stock would represent approximately 4.8 percent of the economic value of Hughes.³⁵

f. Effect of the stock split.³⁶

³² Both the numerator and denominator of the Class H fraction are adjusted quarterly. General Motors Quarterly Report for the Quarterly Period Ending March 31, 2000, SEC Form 10-Q, at 37. The most recent adjustment of these numbers was reported in the General Motors Quarterly Report for the first quarter of 2000. *Id.* The numbers reported in the General Motors Quarterly Report were used to estimate the percentage of the economic value of Hughes that is presently tracked by the GMH stock, and the percentage of the economic value of Hughes that would be tracked by the GMH stock upon conversion of the AOL Series H Preference Stock.

³³ *See supra* note 24.

³⁴ Exchange Offer, at 126.

³⁵ For the purposes of this estimate, we divided 21,529,255 (the number of shares of GMH stock which AOL would hold if it had converted its Preference Stock to GMH stock before the Mandatory Conversion Date) by 453,029,255 (the denominator for the first quarter plus the additional AOL shares) (431,500,000 + 21,529,255).

³⁶ As noted above, on June 6, 2000, GM announced a 3 for 1 stock split of GMH stock. GM Announces Three-For-One Split of Class H Stock, June 6, 2000. The stock split will be in the form of a 200 percent stock dividend payable on June 30, 2000 to GMH stockholders of record on June 13, 2000. *Id.*

i. What effect will the GMH 3 for 1 stock split have on the value of AOL s Preference Stock?

None. The Certificate of Designations provides for an adjustment of the Exchange Rate and the Optional Conversion Rate if GM pays or makes a dividend or other distribution with respect to its GMH stock in shares of GMH stock.³⁷

ii. Will it increase the number of AOL s possible GMH shares?

Yes. As discussed above, the Certificate of Designations provides for the increase of the rate at which AOL s Series H Preference Stock is converted to GMH stock as a result of the stock split.³⁸

iii. If so, if AOL were to convert its Preference Stock today, how many shares of GMH stock would it have?

As discussed above, if AOL were to convert its Series H Preference Stock today, it would receive 21,529,255 shares of GMH stock. However, taking into account the upcoming stock split and the impending adjustment in the Optional Conversion Rate as a result of this split, we estimate that AOL would receive 64,587,766 shares of GMH stock.³⁹

iv. After the GMH 3 for 1 stock split, and upon conversion of its Preference Stock to GMH stock, what will AOL s percentage voting interest in General Motors constitute?

AOL presently does not have a voting interest in GM. If AOL converted its Series H Preference Stock to GMH stock, its percentage voting interest in GM currently would be

³⁷ Certificate of Designations, at Section 6(iii)(a). The Exchange Rate and the Optional Conversion Rate are each increased by multiplying such rate by a fraction the numerator of which is the sum of the number of shares of GMH stock outstanding at the time and date fixed for the determination of stockholders entitled to receive the stock dividend plus the total number of shares of GMH stock constituting the dividend; and the denominator of which is the number of shares of GMH stock outstanding at the time and date fixed for such determination. *Id.* As noted above, we have calculated the number of shares of GMH stock outstanding to be 290,950,014. *See supra* note 18. Using this number, we estimate that the Optional Conversion Rate would become 24.1935. The numerator of the fraction would be the sum of 290,950,014 + 581,900,028. The denominator of the fraction would be 290,950,014. Thus, the Optional Conversion Rate of 8.0645 would be multiplied by 3.

³⁸ *Id.*

³⁹ The product of 2,669,633 (the number of shares of Series H Preference Stock which AOL holds) and 24.1935 (the adjusted Optional Conversion Rate) is 64,587,766.

approximately 1.8 percent.⁴⁰ Under the Certificate of Incorporation, if GM pays a stock dividend in shares of GMH stock to GMH stockholders, GM will adjust the voting rights of shares of GMH stock relative to the common stock so as to avoid the dilution in any aggregate voting rights of any class.⁴¹ Thus, the stock split should not affect the voting rights of GMH common stockholders relative to GM common stock holders. Accordingly, after the stock split and upon conversion of its Series H Preference Stock, AOL's percentage voting interest in GM should remain 1.8 percent. To our knowledge, however, GM has not publicly announced how it will adjust the voting rights of GMH stockholders.

v. What percentage of GMH stock would AOL's GMH shares constitute?

If AOL receives 64,587,766 shares of GMH stock upon conversion of its Series H Preference Stock, and the impending split of the shares of GMH stock outstanding on June 13, 2000 has occurred, AOL will have 6.9 percent of the outstanding shares of GMH stock.⁴² As noted above, however, the GMH stock, even taking the exchange offer, contribution and split into account, tracks only a portion of the economic value of Hughes and thus AOL's interest in the financial performance of Hughes would not exceed five percent.

g. Please produce documents to support your answers to questions in this paragraph.

As noted above, the parties are providing documents in response to this request under separate cover letter.

1.3 Please identify all matters on which only GMH shareholders may vote. Please produce documents to support your response to this request.

GMH stock votes separately as a class only on any amendment to the GM Certificate of Incorporation which adversely affects the rights, powers or privileges of the GMH common stock or

⁴⁰ Presently, each holder of GM common stock is entitled to one vote for each share of GM common stock that he owns; and each holder of GMH common stock is entitled to 0.6 votes for each share of GMH common stock that he owns. Exchange Offer, at 129. Thus, stockholders of GM common stock will have a total of 534,784,403 votes. $(534,784,403)(1) = 534,784,403$ Stockholders of GMH common stock will have a total of 187,487,561 votes. $((290,950,014 + 21,529,255)(0.6) = 187,487,561)$ AOL will have 12,917,553 of these votes. $((21,529,255)(0.6) = 12,917,553)$ Thus, AOL will have a 1.8 percent voting interest in GM. $(12,917,553 \text{ divided by } (534,784,403 + 187,487,561) \text{ equals to } 0.018 \text{ or } 1.8 \text{ percent.})$

⁴¹ Certificate of Incorporation, Article Fourth, Division(I)(e)(1).

⁴² $64,587,766 \text{ divided by } ((290,950,014)(3) + 64,587,765) \text{ equals } 0.069 \text{ or } 6.9 \text{ percent.}$

increases the number of authorized shares of GMH common stock.⁴³ As noted above, the parties are providing documents in response to this request under separate cover letter.

1.4 How are the directors of Hughes and DirecTV elected? Do GMH shareholders have the right to vote for the board of directors of Hughes and/or DirecTV?

GMH shareholders do not have the right to vote for the board of directors of Hughes or DirecTV. Hughes Electronics Corporation is a wholly owned subsidiary of General Motors Corporation. According to the Hughes Bylaws, Hughes stockholders elect its directors.⁴⁴ As GM is the sole stockholder of Hughes, GM elects Hughes directors. DirecTV is a wholly owned subsidiary of Hughes Electronics Corporation. It is AOL's understanding that Hughes, as the sole stockholder of DirecTV, elects DirecTV's directors.

1.5 Please produce the agreement of strategic alliance between AOL and Hughes to which you refer on pages 10-11 of your SI.

As noted above, the parties are providing documents in response to this request under separate cover letter.

Deployment of New Services

The Commission's request for further information next posits a series of questions seeking a description of ownership interests held by Time Warner and AOL in entities providing telephony service as well as information and documents relating to Time Warner's pre-merger and post-merger plans for the deployment of three general categories of new services: local telephony, high-speed Internet access and digital cable television services. Among other things, the Commission is seeking information relating to the planned and actual investment in each category. Thus, for each category, Time Warner's response provides information relating to relevant incremental capital expenditures. For example, in the area of digital cable services, such incremental capital expenditures would include certain headend upgrades and purchase of digital set-top boxes.

Focusing exclusively on Time Warner's incremental capital expenditures and budgets, however, does not provide a complete picture of the level of Time Warner's investment in the provision of new services. Rather, a more accurate analysis would start with Time Warner's substantial embedded investment in its cable television infrastructure. But more specifically, the successful roll-out of each category of service identified by the Commission's request is entirely dependent upon Time Warner's investment to upgrade its cable television infrastructure from essentially an analog, coaxial, tree-and-branch design to a digital enabled, hybrid fiber/coax (HFC), fiber-to-the-node architecture.

⁴³ Certificate of Incorporation at Article 4, Division I(b).

⁴⁴ Hughes Electronics Corporation By-Laws Dated as of May 2, 1999.

Traditional cable systems were initially constructed to provide one-way transmission of video programming services. The capabilities of those coaxial systems are being improved with -HFC systems consisting of a mix of fiber-optic and coaxial lines. In an upgraded system, a fiber-optic line travels from the cable headend to a node -- a connection point in a cable system where a fiber line enters a neighborhood and is then connected to coaxial cables -- which generally serves 200-1000 individual homes. See Broadband Today, A Staff Report to William E. Kennard, Chairman, Federal Communications Commission, October 1999. The replacement of coaxial cable with fiber-optic cable increases the system s capacity and reduces noise, providing cleaner transmission paths that are necessary for two-way interactivity, telephony, and other new services. Id.

As the Commission is aware, in accordance with the undertakings of Time Warner Cable (TWC) pursuant to its Social Contract, TWC is in the final year of a five-year program to substantially upgrade its cable systems. As reported in its 1999 Social Contract Progress Report (copy enclosed), at the end of 1999, TWC s cumulative investment in upgrading and rebuilding its cable systems was \$3.7 billion. This investment has affected approximately 9 million customers who are now being served by upgraded plant in franchises where upgrades have been totally or partially completed. These customers are already benefitting from increased services and programming choice and enhanced system reliability and picture quality. TWC expects to complete its system upgrade obligations under the Social Contract by the end of this year.

1.6 Describe Time Warner s local telephony roll-out plans and (if applicable) its actual roll-out of such services for the following periods:

- a. **pre-merger (*i.e.*, from January 1, 1998, to the date of the Merger Agreement);**
- b. **the present (*i.e.*, from the date of the Merger Agreement to the present);**
- c. **post-merger (*i.e.*, after consummation of the merger, assuming it is approved). Please specifically state how the merger would change Time Warner s prior rollout plans.**

In responding to the foregoing, please identify the geographic areas that Time Warner planned to serve, actually serves, and plans to serve in the future; describe the means of offering local telephony (*e.g.*, resale of ILEC services, facilities-based service); quantify the planned and actual investment in this service; and quantify the planned and actual number of homes passed and subscribers served or planned to be served by systems offering this service.

Residential Telephony

TWC's local residential roll-out plans and (where applicable) actual roll-out of such services are set forth below:

a. pre-merger (i.e., from January 1, 1998 to the date of the Merger Agreement):

TWC completed a first-generation, equipment-only facilities-based trial of residential, IP-based non-powered two-way voice service in Portland, Maine in 1999. During 1999 (year one of the trial), this trial was limited to a small number of homes, and was not marketed to customers. TWC also undertook a facilities-based residential, IP-based service trial in Rochester, New York, which also includes Road Runner high-speed Internet service. This trial was intended to supplement TWC's residential circuit-switched, facilities-based service to several thousand customers in Rochester that commenced in 1994.

Time Warner Connect (formerly KBL Integrated Services) was founded in 1993 to offer local and long distance telephone service, as well as cable television and intrusion alarm systems, to multiple dwelling unit residents.

In addition, in February 1999, Time Warner and AT&T agreed upon a preliminary letter of intent for a cable telephony joint venture. The proposed terms of such venture are described in Time Warner's public filings with the Securities and Exchange Commission. See Time Warner Inc. 10-K, SEC File #:001-12259 (March 26, 1999), at I1-2, F17-18. The terms of that letter of intent called for the negotiation and execution of definitive documents to create the joint venture, and that has not occurred, but discussions with AT&T regarding the provision of residential telephony to cable subscribers remain ongoing.

During 1998 and 1999 TWC reported a total capital investment related to residential telephony of \$_____.

b. the present (i.e., from the date of the Merger Agreement to the present):

In Rochester, New York, TWC currently provides residential circuit-switched service to approximately ___ customers. In Portland, Maine, TWC's second-generation trial of residential, IP-based non-powered voice service does not yet include marketing and product positioning. During 2000 (year 2 of the trial), TWC expects to do so, as to its Road Runner Internet service subscribers, who make up approximately 15 - 20 percent of TWC's cable subscribers in the area. As of February 2000, Time Warner Connect had received state CLEC certifications from California, Florida, Ohio, and Texas. Additionally, as described above, Time Warner and AT&T continue to have discussions regarding cable telephony. On March 8, 2000, TWC and AT&T announced a joint marketing agreement. Pursuant to this arrangement, incentives are being offered to consumers in Albany and Syracuse, NY who choose both TWC cable service and AT&T communications service.

c. post-merger (i.e., after consummation of the merger):

Going forward, TWC expects to continue providing circuit-switched service in Rochester, New York. In Portland, Maine, TWC plans to proceed with marketing IP non-powered voice service to its Road Runner subscribers on a trial basis. Pending analysis of the results of these trials, TWC has no definitive plans for further roll-outs. TWC and AT&T also expect to expand their joint marketing arrangement, by offering other incentives to customers of long distance and cable service, and engaging in joint telemarketing efforts.

Given TWC's technologically advanced cable systems and residential plans focused on IP technology, and AOL's leadership in making the Internet consumer-friendly, the parties expect to combine their skills to learn from TWC's trials of residential IP voice service over cable plant, in order to maximize the potential for a more rapid and widespread deployment of this service. Indeed, AOL and Time Warner have already held discussions to explore potential synergies in such areas as residential IP telephony, long distance, and wireless services.

Business Telephony

As detailed in response to item 1.8, Time Warner holds a 47.85 percent equity interest in Time Warner Telecom Inc. (TWT), a publicly-traded corporation. TWT is a leading fiber facilities-based integrated communications provider offering local business last mile broadband connections for data, high-speed Internet, local voice and long distance services. TWT offers a wide range of business telephony services, primarily to medium- and large-sized telecommunications-intensive business end-users, long distance carriers, Internet service providers, wireless communications companies and governmental entities. These business telephony services include dedicated transmission, local switched, long distance, data and video transmission services and high-speed dedicated Internet services.

TWT's dedicated services, including private line and special access services, use high-capacity digital circuits to carry voice, data and video transmissions from point-to-point in multiple configurations. TWT's switched voice services use high-capacity digital switches to route voice transmissions anywhere on the public switched telephone network. TWT also provides private network management and systems integration services for businesses that require combinations of various dedicated and switched telecommunications services. Data services provided by TWT allow customers to create their own internal computer networks and access external computer networks and the Internet. TWT's video transport services provide customers with advanced services such as point-to-point, broadcast-quality video. TWT's Internet services include dedicated Internet access, website hosting, transport and e-commerce for business customers and local Internet service providers.

TWT's facilities-based local business telephony rollout plans and (where applicable) actual rollout of such services is as follows:

a. pre-merger (i.e., from January 1, 1998 to the date of the Merger Agreement)

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As of January 1, 1998, TWT operated networks in 19 metropolitan areas covering 5,913 route miles, 233,488 fiber glass miles and offered service to 2,426 buildings. These 19 metropolitan areas are grouped in six regional clusters, as follows:

New York Region

Albany, NY
Binghamton, NY
Manhattan, NY
Rochester, NY

Southwest Region

Austin, TX
Houston, TX
San Antonio, TX
San Diego, CA

Southeast Region

Charlotte, NC
Greensboro, NC
Memphis, TN
Raleigh, NC

Midwest Region

Cincinnati, OH
Columbus, OH
Indianapolis, IN
Milwaukee, WI

South Region

Tampa, FL
Orlando, FL

Hawaii Region

Honolulu, HA

As of January 1, 1998, TWT deployed switches in 14 of these areas. As of March 31, 1998, TWT's networks spanned 6,240 route miles, contained 244,894 fiber glass miles and offered service to 2,711 buildings with 1,904,420 VGE circuits and 23,702 access lines in service. As of December 31, 1998, TWT increased to 16 the number of metropolitan areas in which it offered switched services. TWT's investment in its communications networks during 1998 was over \$380 million. During 1999, TWT added two service areas, Dallas, Texas and Jersey City, New Jersey, for a total of 21, and increased to 19 the number of areas where it deployed digital telephony switches. As of December 31, 1999, TWT's network included 8,872 route miles, 332,263 fiber miles and offered service to 5,566 buildings. During 1999, TWT's investment in its communications networks was over \$556 million.

b. the present (i.e., from the date of the Merger Agreement to the present):

TWT is in the process of constructing three additional networks during 2000: Los Angeles/Orange County, California; Dayton, Ohio; and Fayetteville, North Carolina. Additionally, TWT is in the process of interconnecting its 21 existing areas within regional clusters with owned or licensed fiber optic facilities, which is expected to address customers regional long distance voice, data and video requirements. TWT now offers switched services in 20 out of its 21 service areas. Based on historic capital requirements for network construction in relation to sales volumes and network expansion plans, TWT anticipates it will commit approximately \$350 million in 2000 to fund its capital expenditures. This includes requirements for current operating areas and TWT's expansion plans.

c. post-merger (i.e., after consummation of the merger):

TWT expects a geographic expansion plan that presently calls for commencing construction in an additional 8 to 12 metropolitan statistical areas during 2000 and 2001. The first phase of this planned expansion includes Denver, Colorado; Atlanta, Georgia; Chicago, Illinois; Minneapolis, Minnesota; and Columbia, South Carolina, which are expected to be operational in 2001. TWT has also indicated that it will evaluate other expansion opportunities. As part of this process, TWT is targeting the expansion of data and Internet products that can be offered on TWT's existing network. TWT does not anticipate that its deployment plans will be affected by the AOL/Time Warner merger.

1.7. Please provide all documents relating to the telephony plans discussed in your response to request 1.6.

As noted above, the parties are providing documents in response to this request under separate cover letter.

1.8 Describe and quantify all AOL or Time Warner ownership interests and voting and management rights in entities providing any kind of telephony service, whether local or long distance, circuit-switched or packet-switched (e.g., Net2Phone), and describe and quantify the ownership interests and voting and management rights of all other entities holding ownership interests of 5% or more in those entities.

Time Warner

TWC holds ownership interests in the following entities created to provide telephony services:

Time Warner AxS of Northeast Ohio
L.P. Time Warner AxS of Western Ohio
L.P. Time Warner Rescom of New York LLC

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Time Warner Rescom of Texas, L.P.
Time Warner Connect
Time Warner Connect of San Antonio Inc.

Time Warner AxS of Northeast Ohio, L.P. and Time Warner AxS of Western Ohio, L.P. are Delaware limited partnerships each 99 percent owned by Time Warner Entertainment Company, L.P. (TWE) and one percent owned by the general partner, Time Warner Cable Holdings, Inc. (TWCHI), a Delaware corporation owned 100 percent by TWE. TWE is a partnership of Time Warner and MediaOne Group, Inc. (MediaOne).⁴⁵

Time Warner Rescom of New York LLC is a Delaware limited liability company 50 percent owned by TWE and 50 percent owned by Time Warner Entertainment-Advance/Newhouse Partnership (TWE-A/N). TWE-A/N is a partnership of TWE, Time Warner and Advance/Newhouse Partnership (Advance).

Time Warner Rescom of Texas, L.P. is a Texas limited partnership one percent owned by its general partner TWEAN Holdings Inc., 49 percent owned by TWE-A/N and 50 percent owned by Texas Cable Partners, L.P. TWEAN Holdings Inc. is a Delaware corporation 100 percent owned by TWE-A/N. Texas Cable Partners, L.P. is a Delaware limited partnership 49.5 percent owned by TCI Texas Cable Holdings LLC, a Colorado limited liability company 100 percent owned by AT&T Corp., 49.5 percent owned by TWE-A/N, .5 percent owned by TCI Texas Cable Inc., a Colorado corporation 100 percent owned by AT&T Corp. and .5 percent owned by TWE-A/N Texas Cable Partners General Partner LLC, a Delaware limited liability company 100 percent owned by TWE-A/N.

Time Warner Connect is a New York general partnership 99 percent owned by Time Warner Service Holdings I, L.P., a Delaware limited partnership, and 1 percent owned by Time Warner Service Holdings II, L.P., a Delaware limited partnership. These entities are wholly owned by Time Warner. Time Warner Connect of San Antonio, Inc. is a Delaware corporation, wholly owned by Time Warner.

TWT is a publicly traded corporation in which Time Warner indirectly holds 47.85 percent of the equity and 66.68 percent of the voting power. TWT holds certificates to provide telecommunications services in 12 states, which include 21 metropolitan areas. TWT began by providing telephony services through cable television systems owned by TWE, TWE-A/N and Time Warner. On July 14, 1998, TWT LLC succeeded to the ownership of TWT's business. On May 14, 1999, TWT LLC was reconstituted as a Delaware corporation under the name Time Warner Telecom Inc.

TWT's authorized capital includes two classes of Common Stock, Class A Common Stock, which is held by the public, and Class B Common Stock, which is held by Time Warner, Advance and MediaOne. Each share of Class B Common Stock is convertible, at the option of the holder, into one

⁴⁵ On June 15, 2000, AT&T Corp. completed its acquisition of MediaOne.

share of Class A Common Stock. As of May 2, 2000, the Class B stockholders had approximately 95.6% of the combined voting power of the outstanding Common Stock in TWT. Holders of TWT Class A Common Stock and Class B Common Stock generally vote together as a single class. However, the differences between these classes are:

1. holders of Class A Common Stock are entitled to one vote per share, and holders of Class B Common Stock are entitled to 10 votes per share on all matters submitted to a vote of shareholders;
2. certain matters require the approval of 100 percent of the outstanding Class B Common Stock, voting separately as a class; and
3. certain other matters require the approval of a majority of the outstanding Class A Common Stock, voting separately as a class.

Time Warner owns a 66.68 percent voting and 47.85 percent equity interest in TWT, in Class B Common Stock. Advance owns a 20.62 percent voting and 14.8 percent equity interest in TWT, in Class B Common Stock. MediaOne owns an 8.33 percent voting and 5.98 percent equity interest in TWT, in Class B Common Stock, as is more fully explained below. The remaining 4.37 percent voting interest in TWT is publicly held, in Class A Common Stock, along with their 31.3 percent equity interest.

Management of TWT is accountable to its board of directors (the Board). TWT's Board consists of seven directors. Time Warner has the right to designate three nominees for the Board, and Advance has the right to designate one nominee. Two directors are independent, and the seventh is TWT's Chief Executive Officer.

TWT owns a 99 percent interest in the state and regional operating entities that operate the TWT networks described above. The remaining 1% interest is owned by Time Warner Telecom Holdings, Inc., which is wholly owned by TWT. These operating entities are as follows:

- Internet Connect, Inc.
- MetroComm AxS, L.P.
- Time Warner Telecom of California, L.P.
- Time Warner Telecom of Florida, L.P.
- Time Warner Telecom of Georgia, L.P.
- Time Warner Telecom of Hawaii, L.P.
- Time Warner Telecom of Indiana, L.P.
- Time Warner Telecom of Illinois, L.P.
- Time Warner Telecom of New Jersey, L.P.
- Time Warner Telecom of North Carolina, L.P.
- Time Warner Telecom-NY, L.P.
- Time Warner Telecom of Ohio, L.P.
- Time Warner Telecom of Texas, L.P.
- Time Warner Telecom of The Mid-South, L.P.
- Time Warner Telecom of Wisconsin, L.P.

On May 1, 2000, MediaOne closed the sale of 9 million of its shares in TWT, and along with such sale, its financial interest in TWT had been reduced to less than 10 percent, and it lost the right to appoint directors to TWT's board. MediaOne's board representatives resigned in connection with this sale of shares. MediaOne has stated that it continues to own 6,289,842 shares of TWT Class B stock, which represent less than 6 percent of TWT's total outstanding shares and less than a 10 percent voting interest in TWT.

During the second quarter of 1999, TWT acquired all of the outstanding common stock of MetroComm, Inc. through the issuance of 2,190,308 shares of TWT Class A Common Stock valued at \$24.1 million, and the assumption of \$20.1 million in liabilities. Through the acquisition of MetroComm, TWT acquired the 50 percent interest of MetroComm AxS, L.P., a competitive local exchange carrier in Columbus, Ohio, not already owned by TWT.

AOL

As for AOL's response to this question, AOL has ownership interests and voting and management rights in the following two companies: (1) Talk.com Inc. (formerly Tel-Save.com, Inc., hereinafter "Talk.com") and (2) Net2Phone, Inc. ("Net2Phone").

Talk.com

Talk.com, through its subsidiaries, provides telecommunications services to residential and business customers throughout the United States, primarily through its e-commerce platform, which uses online and web-enabled customer care, billing and information systems. Talk.com's telecommunications services include long distance outbound service, inbound toll-free service and dedicated private line services for data. Talk.com offers local telecommunications services in various states and has announced plans to offer a bundle of long distance and local service to small business and select residential customers in nine southeastern states serviced by Access One Communications Corp., a private local telecommunications service provider that is being acquired by Talk.com, subject to stockholders and regulatory approvals.⁴⁶

AOL's Ownership Interest

AOL owns 4,121,372 shares of Common Stock of Talk.com, which represents 6.26 percent of the total outstanding shares of Common Stock as reported by Talk.com in its SEC Form 10-Q, filed on May 15, 2000.⁴⁷

⁴⁶ Talk.com currently offers local telecommunications service in Florida, Georgia, North Carolina, and New York. See Talk.com SEC Form 10-Q, Quarterly Report, filed May 15, 2000.

⁴⁷ Talk.com's SEC Form 10-Q reports that there were 65,819,573 shares of Common Stock outstanding as of May 2, 2000. AOL also holds warrants to acquire an additional 2,721,984 shares of Common Stock of Talk.com.

AOL s Management and Voting Rights

The voting and management rights of Talk.com are governed by the laws of Delaware. AOL has entered into an Investment Agreement with Talk.com dated as of December 31, 1998 (as amended February 22, 1999 and August 1999) that gives AOL certain rights with respect to the shares and warrants it owns, and imposes certain restrictions on Talk.com. The restrictions on Talk.com include a restriction on incurrence of indebtedness and a limitation on Talk.com entering into transactions with any person that owns more than 15 percent of the issued and outstanding shares of Talk.com unless a majority of the disinterested directors of Talk.com approve the transaction. The Investment Agreement provides that AOL will have the right to sell its shares (and warrants and shares received on exercise of warrants) back to Talk.com at certain times and at specified prices, or to receive reimbursement from Talk.com if AOL sells shares on the market for less than the specified prices. Finally, the agreement provides that AOL's rights to sell shares and warrants or to receive reimbursement will accelerate if Talk.com takes certain actions including: undergoing a Change of Control (as defined in certain debt instruments of Talk.com); retaining a specified person as an executive officer of Talk.com; breaching its agreements under the Investment Agreement or a Telecommunications Marketing Agreement with AOL; or committing a material default under its debt agreements.

Five Percent or Greater Ownership Interests and Management and Voting Rights

AOL s knowledge relating to persons or entities with five percent or greater ownership interest in Talk.com is based on Talk.com s publicly available filings with the Securities Exchange Commission. Talk.com s SEC Form 10-Q, Quarterly Report, filed on May 15, 2000 indicates that 65,819,573 shares of Common Stock were issued and outstanding as of May 2, 2000. Thus, based on Talk.com s SEC Form 10-K/A, Amended Annual Report, filed on April 28, 2000, the other persons or entities that have a five percent or greater ownership interest in Talk.com are as follows:

Massachusetts Financial Services Company
500 Boylston Street
Boston, Massachusetts 02116

Legg Mason, Inc.
100 Light Street
P.O. Box 1476
Baltimore, Maryland 21203

Paul Rosenberg
650 N.E. 5th Avenue
Boca Raton, Florida 33432

Geocapital, LLC
767 Fifth Avenue, 45th Floor
New York, New York 10153

Net2Phone

Net2Phone is a provider of services, commonly known as Internet telephony or IP telephony, that enable users to make high-quality, low-cost telephone calls over the Internet. Net2Phone's IP telephony services enable end users to call individuals and business worldwide using personal computers or traditional telephones. Net2Phone also provides technology to integrate live voice capabilities into the Web.

AOL's Ownership Interests

AOL owns 2,750,000 shares of Net2Phone, representing 2,250,000 shares of Class A Common Stock (each share of which entitles its holder to two votes) and 500,000 shares of common stock (each share of which entitles its holder to one vote). AOL's 2,250,000 shares of Class A Common Stock represent 6.63 percent of Net2Phone's outstanding Class A Common stock. AOL's 500,000 shares of Common Stock represent 2.33 percent of Net2Phone's outstanding Common Stock.⁴⁸ AOL has sole voting and sole dispositive power with respect to all such shares. Pursuant to a Stockholders Agreement dated May 13, 1999, by and among IDT Corporation (IDT), Clifford Sobel, Net2Phone and certain other investors (the Net2Phone Stockholders Agreement), AOL may not, without Net2Phone's consent, transfer its shares of Net2Phone to any person or entity which derives a majority of its revenue from providing Internet telephony services until 2002.

AOL's Management and Voting Rights

The voting and management rights of Net2Phone are governed by Net2Phone's Certificate of Incorporation and Bylaws and Delaware law. Pursuant to Net2Phone's Certificate of Incorporation, holders of its Class A Common Stock are entitled to two votes per share and holders of Common Stock are entitled to one vote per share. AOL's ownership interest represents 5.6 percent of the voting power based upon the number of shares outstanding of Common Stock as reported by Net2Phone's Form DEF 14A, Definitive Proxy Statement filed on June 6, 2000. Class A Common stock automatically converts into Common Stock with one vote per share upon any transfer unless the transferee is a permitted transferee under Net2Phone's corporate charter, the definition of which includes other holders of Class A Common Stock. Net2Phone's Certificate of Incorporation also provides that the affirmative vote of the holders of at least 66 and 2/3 percent of the outstanding shares of Class A Common Stock and Common Stock, voting as a single class, is required to approve

⁴⁸ AOL's total ownership interest represents 4.97% of Net2Phone's Common Stock, based upon the number of shares of Common Stock outstanding as reported by Net2Phone's SEC Form DEF 14A, Definitive Proxy Statement, filed on June 6, 2000. Net2Phone's SEC Form DEF 14A reports that there were 33,924,250 shares outstanding of Class A Common Stock and 21,420,473 shares outstanding of Common Stock. AOL also owns an unvested warrant to purchase, at specified prices, up to 4.5% of the fully-diluted shares of Net2Phone's outstanding Common Stock at the time of exercise. That warrant vests upon AOL's achievement of specified performance hurdles relating to revenues received by Net2Phone as a result of AOL's promotion of Net2Phone's services.

(1) any sale of all or substantially all of the property and assets of Net2Phone; (2) any action taken to dissolve Net2Phone; (3) any merger of Net2Phone with another company in which the holders of Net2Phone's equity securities immediately prior to the closing of such transaction become the beneficial owners of 50 percent or less of the voting equity securities of the surviving entity; (4) any change in authorized capital; or (5) the removal of a director other than for cause. Pursuant to the Net2Phone Stockholders Agreement, AOL and other investors have agreed to elect a nominee from each of Softbank Technology Ventures IV, L.P. and GE Capital Equity Investments Inc. to the board of directors of Net2Phone. In addition, a representative of AOL is entitled to attend all Net2Phone board meetings in a nonvoting observer capacity.

Five Percent or Greater Ownership Interests and Management and Voting Rights

AOL's knowledge of entities with five percent or greater ownership interest in Net2Phone is based on Net2Phone's publicly available filings with the Securities and Exchange Commission. Please see attached chart for information regarding these entities. Based on information reported in Net2Phone's SEC Form DEF 14A, Definitive Proxy Statement, filed on June 6, 2000, the entities with five percent or greater ownership interest in Net2Phone are as follows:

IDT Corporation.
190 Main Street
Hackensack, New Jersey 07601

SOFTBANK Technology Ventures IV, L.P.
333 West San Carlos Street, Suite 1225
San Jose, California 95110

Yahoo! Inc.
3420 Central Expressway
Santa Clara, California 95051

AT&T Agreement

On March 30, 2000 Net2Phone entered into an agreement with AT&T Corp. (AT&T) and IDT.⁴⁹ If approved at a Special Meeting of Stockholders to be held on July 6, 2000, AOL's ownership and voting power in Net2Phone would be diluted. Pursuant to the terms of the agreement, Net2Phone, subject to stockholder approval and the satisfaction of other conditions, will issue 4,000,000 newly-authorized shares of its Class A Common Stock to a newly formed corporation controlled by AT&T. In addition, the agreement between AT&T and IDT provides that AT&T, upon Net2Phone's stockholders' approval and satisfaction of the other conditions in the agreement, purchase 14.9 million shares of Net2Phone Class A Common Stock currently owned by IDT. Upon consummation of these transactions:

⁴⁹ See Net2Phone SEC Form DEF 14A, Definitive Proxy Statement (filed June 6, 2000).

- AT&T will, through its wholly-owned subsidiary, own approximately 32 percent of Net2Phone s outstanding capital stock, and will control 39 percent of the aggregate voting power of Net2Phone s capital stock.
- AOL s ownership of Net2Phone s outstanding capital stock will be reduced from 4.97 percent to 4.63 percent, and its voting power will be reduced from 5.6 percent to 5.14 percent.
- AT&T s wholly-owned subsidiary and IDT will enter into a voting agreement with respect to the election of mutually acceptable nominees to the Board. So long as they agree on nominees, AT&T s wholly-owned subsidiary and IDT will collectively control approximately 60 percent of Net2Phone s voting power and will therefore likely control the election of all of Net2Phone s directors; however, if they are unable to agree on acceptable nominees, the votes of other stockholders will determine the election of Net2Phone s directors. This agreement terminates by its terms no later than August 1, 2003.
- Initially, AT&T, through its wholly-owned subsidiary, also will have the right to designate three individuals to be appointed as directors on Net2Phone s Board, one of whom shall be elected to fill the vacancy created by the resignation of a director currently designated by IDT. AT&T s wholly-owned subsidiary and IDT has each agreed to use its best efforts, so long as it beneficially owns between 15 percent and 85 percent of Net2Phone s voting power, to assure that Net2Phone s Board consists of at least 5 directors who are not employees of or affiliated with Net2Phone, IDT, AT&T or any of their affiliates. These independent directors will take action on behalf of the Net2Phone Board on matters involving or relating to its relationship with IDT, AT&T and other interested parties.

1.9 Describe Time Warner s roll-out plans and (if applicable) its actual roll-out of high speed Internet access services for the following periods:

- a. **pre-merger (i.e., from January 1, 1998, to the date of the Merger Agreement);**
- b. **the present (i.e., from the date of the Merger Agreement to the present);**
- c. **post-merger (i.e., after consummation of the merger, assuming it is approved). Please specifically state how the merger would change Time Warner s prior rollout plans.**

In responding to the foregoing, please identify the geographic areas that Time Warner planned to serve, actually serves, and plans to serve in the future; quantify the planned and actual investment in this service; and quantify the planned and actual number of homes passed and subscribers served or planned to be served by systems offering this service.

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Time Warner provides cable service (including high speed Internet service) through Time Warner Cable (TWC), which manages its cable systems. TWC is a division of Time Warner Entertainment Company, L.P. (TWE). TWC s divisions are organized geographically across the country in 40 divisions:

Albany, NY
Austin, TX
Bakersfield, CA
Binghamton, NY
Birmingham, AL
Charlotte, NC
Cincinnati, OH
Columbus, OH
Desert Cities (CA)
El Paso, TX (a.k.a. Paragon Southwest)
Florida
Green Bay, WI
Greensboro, NC
Hawaii
Houston, TX
Indianapolis, IN
Jackson, MS/Monroe, LA
Kansas City, MO
Liberty (NY)
Lincoln, NE
Los Angeles, CA
Memphis, TN
Milwaukee, WI
Minneapolis, MN (a.k.a. Minnesota)
National⁵⁰
New York City
Northeast Ohio
Portland, ME (a.k.a. New England)
Raleigh/Durham, NC
Rochester, NY
San Antonio, TX
San Diego, CA
Shreveport, LA
South Carolina (a.k.a. Columbia)
Staten Island, NY
Syracuse, NY

⁵⁰ The National division is comprised of smaller systems located in Alabama, Florida, Georgia, Indiana, Kansas, Louisiana, Michigan, Mississippi, New Hampshire, New Jersey, Oklahoma, Pennsylvania, Texas and West Virginia.

Tampa Bay, FL
 Waco, TX
 Western Ohio
 Wilmington, NC

a. Pre-merger high speed Internet service roll-out status:

As of the week ending January 8, 2000, TWC had rolled out high speed Internet service in the following divisions:

<u>Division</u>	<u>Cable Modem Customers</u>	<u>Cable Modem Ready Homes passed</u>
Albany		
Austin		
Binghamton		
Charlotte		
Cincinnati		
Columbus		
El Paso		
Florida		
Greensboro		
Hawaii		
Houston		
Kansas City		
Los Angeles		
Memphis		
New York City		
N.E. Ohio		
Portland		
Rochester		

<u>Division</u>	<u>Cable Modem Customers</u>	<u>Cable Modem Ready Homes passed</u>
San Antonio		
San Diego		
S. Carolina		
Syracuse		
Tampa Bay		
TOTAL		

b. High speed Internet roll-out status since the announcement of the merger:

Subsequent to the announcement of the merger, TWC has rolled out high speed Internet service to an additional four divisions. The roll-out status as of the week ending May 20, 2000 is set forth below:

<u>Division</u>	<u>Cable Modem Customers</u>	<u>Cable Modem Ready Homes passed</u>
Albany		
Austin		
Binghamton		
Charlotte		
Cincinnati		
Columbus		
El Paso		
Florida		
Greensboro		
Hawaii		
Houston		
Kansas City		

<u>Division</u>	<u>Cable Modem Customers</u>	<u>Cable Modem Ready Homes passed</u>
Los Angeles		
Memphis		
Minnesota		
New York City		
N.E. Ohio		
Portland		
Raleigh		
Rochester		
San Antonio		
San Diego		
S. Carolina		
Syracuse		
Tampa Bay		
Waco		
Western Ohio		
TOTAL		

c. Post-merger roll-out plans:

By the end of 2000, TWC plans that high speed Internet service will be rolled out to the following 12 divisions:

<u>Division</u>	<u>Projected Subs Year-end</u>

2002		
2003		

TWC's five-year incremental (i.e., over and above the plant upgrade costs described above) investment projections for high-speed Internet service are set forth below:

	Subscriber Acquisition⁵¹	Capital⁵²
1999		
2000		
2001		
2002		
2003		

In addition, as described in response item 1.6.c., TWT provides telephony and Internet services primarily to business customers, and its rollout plans for high-speed Internet service thus mirror TWT's telephony rollout plans described above. During the second quarter of 1999, TWT acquired all of the outstanding common stock of Internet Connect, Inc., an Internet service provider to business customers, for consideration consisting of \$3.8 million of Class A limited liability interests in TWT LLC, TWT's predecessor, approximately \$3.5 million in net cash and the assumption of \$1.9 million in liabilities. At the time of TWT's initial public offering in 1999, the Class A limited liability interests were converted into 307,550 shares of Class A Common Stock of TWT. This Common Stock will be held in escrow to be released to the former Internet Connect, Inc.'s shareholders over a three year period. Through the Internet Connect, Inc., acquisition, TWT manages current and future data networks and provides new Internet products.

Time Warner expects the AOL/Time Warner merger to expedite the availability of high-speed Internet service to consumers from multiple providers. First, pursuant to the MOU, Time Warner has agreed to work with its venture partners in Road Runner to achieve an early termination of the provisions of the agreements between Road Runner and Time Warner Cable that restrict the ability to

⁵¹ Includes marketing, PC installations, etc.

⁵² Includes cable modems, additional outlet installations, etc.

provide multiple ISPs. Second, Time Warner has committed, as set forth in the MOU, to negotiate with multiple ISPs towards arrangements whereby consumers will have additional options in obtaining cable modem service. Time Warner firmly believes that a multiple ISP model will lead to higher overall cable modem penetration.

1.10 Please provide all documents relating to the high-speed Internet access plans discussed in your response to request 1.9.

As noted above, the parties are providing documents in response to this request under separate cover letter.

1.11 Describe Time Warner s roll-out plans and (if applicable) its actual roll-out of digital cable television services for the following periods:

- a. pre-merger (*i.e.*, from January 1, 1998, to the date of the Merger Agreement);
- b. the present (*i.e.*, from the date of the Merger Agreement to the present);
- c. post-merger (*i.e.*, after consummation of the merger, assuming it is approved). Please specifically state how the merger would change Time Warner s prior rollout plans.

In responding to the foregoing, please identify the geographic areas that Time Warner planned to serve, actually serves, and plans to serve in the future; quantify the planned and actual investment in this service; and quantify the planned and actual number of homes passed and subscribers served or planned to be served by systems offering this service.

As explained in response to question 1.9, Time Warner Cable (TWC) has 40 divisions, organized geographically across the country. TWC s roll-out of digital cable television services⁵³ is focused on these divisions.

The Pegasus Program is TWC s company-wide project to provide digital cable service, through the deployment of advanced set-top boxes, to its cable subscribers.⁵⁴ The Pegasus Program

⁵³ Given the juxtaposition of questions 1.9 and 1.11, Time Warner construes question 1.11 to focus on roll-out plans related to digital video programming services, and to exclude any other programming services that may fall within the statutory definition of cable service, 47 U.S.C. § 522(6).

⁵⁴ TWC has also deployed advanced broadband services outside of its Pegasus Program in a small number of systems, primarily in Texas, recently acquired from Tele-Communications, Inc. (TCI). In these systems acquired from TCI, TWC has continued to deploy General Instrument Corporation s (General Instrument) DCT 2000 platform that includes TV Guide s Navigator

is divided into two phases. Phase One, the current phase, is the deployment of downstream digital services; the primary customer benefit is access to an increased number of cable service channels. During Phase One, the total number of cable service channels typically increases from 80 analog channels to an additional 100 digitally-delivered channels.

During Phase Two, currently under development, TWC plans to launch the Video On Demand (VOD) service onto the existing digital set-up boxes, utilizing interactivity between the subscriber and the cable system. TWC s current goal is to have the VOD product commercially available during 2000.

a. Pre-merger digital cable service deployment status:

As of December 31, 1999, TWC had installed Pegasus headend components, and rolled-out digital set-top boxes, in the following 29 divisions, representing approximately 70% of TWC s total homes passed:

<u>Division</u>	<u>Digital Subscribers (12/31)</u>
Albany	
Austin	
Bakersfield	
Binghamton	
Charlotte	
Cincinnati	
Columbus	
El Paso	
Florida	
Greensboro	

(formerly Prevue Guide, now TV Guide Interactive). The General Instrument platform was chosen by TCI before TWC acquired the systems and TWC has continued to use the platform already in place. TWC s response to this question focuses only on TWC s own Pegasus deployment, which includes TWC s digital television strategy, but does not include the strategy TWC inherited from TCI.

<u>Division</u>	<u>Digital Subscribers (12/31)</u>
Hawaii	
Houston	
Kansas City	
Liberty	
Los Angeles	
Memphis	
Milwaukee	
Northeast Ohio	
Portland	
Raleigh	
Rochester	
San Antonio	
South Carolina	
San Diego	
Syracuse	
Tampa Bay	
Waco	
Western Ohio	
Wilmington	
TOTAL	

Thus, by the end of 1999, TWC installed over _____ digital set-top boxes company-wide. TWC's total investment in digital set-top boxes during 1999 was \$_____.

b. Digital cable deployment since the announcement of the merger:

Subsequent to the announcement of the merger, TWC has rolled out digital cable service to an additional seven divisions. The deployment status of digital cable service as of the month ending May 31, 2000 is set forth below:

<u>Division</u>	<u>Digital Subscribers (5/00)</u>
Albany	
Austin	
Bakersfield	
Binghamton	
Birmingham	
Charlotte	
Cincinnati	
Columbus	
El Paso	
Florida	
Greensboro	
Hawaii	
Houston	
Kansas City	
Liberty	
Los Angeles	
Memphis	
Minneapolis	
National	
New York City	
Milwaukee	

<u>Division</u>	<u>Digital Subscribers (5/00)</u>
Northeast Ohio	
Portland	
Raleigh	
Rochester	
San Antonio	
South Carolina	
San Diego	
Syracuse	
Tampa Bay	
Waco	
Western Ohio	
Wilmington	
TOTAL	

As of the month ending May 31, 2000, TWC's incremental additional investment for the year 2000 in digital set-top boxes amounted to \$ _____.

c. Post-merger deployment plans:

Although TWC has not made any definitive five-year projections, TWC expects to install _____ digital set-top box units company-wide each year for the next three years. TWC's 1999 Business Plan included the following projections relating to digital cable service roll-out:

<u>Year</u>	<u>Digital Subscribers (Millions)</u>
1999	
2000	
2001	

2002
2003

Time Warner believes that completion of the merger will help accelerate TWC's ongoing roll-out plans for digital cable television services. To date, the most significant variable affecting TWC's ability to rollout digital cable service expeditiously has been the availability of advanced set-top boxes from third party suppliers. TWC understands that AOL has been independently pursuing the design and manufacture by third parties of advanced set-top boxes in connection with its AOL TV project. Time Warner anticipates that, once the merger is completed and AOL and TWC are able to combine their resources, particularly their cumulative expertise with respect to set-top box design and functionality, the pace of deployment of digital cable service by TWC will be accelerated.

1.12 Please provide all documents relating to the digital cable rollout plans discussed in your response to request 1.11.

As noted above, the parties are providing documents in response to this request under separate cover letter.

1.13 According to commenters, AOL originally pledged to work with the instant messaging (IM) industry to create an interoperability standard, but has since ceased participation in the standard setting process. Please provide a narrative response to the following questions.

- a. Is AOL actively working with other IM providers to set standards for interoperability? If not, why? If so, in what capacity?**

AOL pioneered the concept of IM in 1985 and unveiled the first IM service to its members as a feature of the AOL service in 1989. At that time, IM was available only to AOL subscribers. Recognizing the growing popularity of IM, in 1997 AOL began giving away for free its AOL Instant Messenger (AIM) client software to anyone on the web. AOL has also entered more than a dozen royalty-free license agreements with other companies including Lotus, Lycos, EarthLink, and other ISPs to distribute AIM, including cobranded versions, and AOL is working to add even more partners to this list.

In addition, AOL has and continues to support efforts to create an open and interoperable standard that would allow users to exchange instant messages across different IM networks. To that end, AOL has participated in industry discussions through the Internet Engineering Task Force (IETF) about how to best achieve this goal. At the same time, however, AOL has resisted unauthorized attempts to access its network by alternative IM providers that would jeopardize the security and privacy of AOL members and AIM users.

On June 15, 2000, responding to a call from the IETF for industry ideas on IM interoperability, AOL submitted a proposed architectural design for a worldwide IM system. AOL believes that its proposal, a copy of which is attached, represents a significant step toward the ultimate development of detailed protocols for implementing full IM interoperability. AOL's proposed system is specifically designed to address threats to the user experience including offensive spam, attempts to defraud, and virus proliferation by way of a server-to-server approach to interoperability that would work in a manner similar to Internet e-mail. AOL's design would protect user privacy, security, and ease-of-use, promote continued long-term competition and innovation in the industry, and provide the greatest degree of scalability. Specifics include the following:

- Full Interoperability** The server-to-server architecture of the AOL design would allow users of any two IM networks that use the same protocols to communicate with one another at any time;
- Privacy and Security** Under this architecture, users would need to be registered with only one instant messaging system, and would not be required to share passwords, log-in IDs, or other confidential information with anyone outside the network they choose. In addition, the design includes requirements that IM data could not be easily intercepted or hijacked and that more advanced security measures such as end-to-end encryption or signing could be layered on top of initial implementations. Finally, it would require that individual networks be allowed to use firewalls or other precautions to ensure the highest possible degree of security;
- Scalability** This design would enable the development of any number of IM systems, from large networks like AOL to individual families with their own servers;
- Independence** No government or other central authority would be required to administer the system; and
- User Name Consistency** Users of instant messaging networks would be able to keep their existing screen names or addresses, even if different users had identical names on different networks.

AOL is confident that this proposal will advance the effort to develop and implement IM interoperability standards that abide by its first commitment and biggest concern in this process: protecting the privacy and security of IM users.

- b. Can other IM providers' customers currently connect with AOL's IM customers?**

Today's instant messaging systems are typically comprised of a client, through which the end-user interacts, and servers which relay information between compatible clients. Tight integration between clients and servers allows instant messaging services to provide a secure, reliable channel through which authentication, presence, and messaging information is passed between users and the service.

As a general matter, a consumer who is using one IM service is not able to exchange messages with a consumer who is using another IM service. It should be noted that this is true whether one consumer is using AIM and the other is using an unaffiliated IM service, each is using a different AOL-affiliated IM service (*i.e.*, one is using AIM and the other ICQ), or if both are using different, unaffiliated IM services (*e.g.*, MSN Messenger and Yahoo! Messenger). AOL is hopeful that the IM industry soon will adopt an open IM standard consistent with the proposal recently submitted to the IETF and described above that will allow consumers to safely and securely exchange instant messages no matter what IM provider they use, just as they are able to do with e-mail.

The instant messaging industry today is a dynamic and rapidly growing arena with dozen of companies competing for customers and constantly innovating in order to improve their users experience. In fact, more than 40 different instant messaging and chat programs are available today. These include the following:

<u>Name:</u>	<u>Available On The Web At:</u>
AbbottChat	www.abbottsys.com/atchat.html
ACD Express Communicator	www.acdsystems.com/products/express/expcom.htm
Ahoy!	www.quicomm.com/AHOY/ahoy.html
ChitChat	members.aol.com/chinyu/chitchat
Excite PAL	talk.excite.com/communities/excite/pal
Goody	www.goody.com
ichat Pager	www.ichat.com
Infoseek Messenger	www.peoplelink.com/v1/down_infoseek
Jabber	jabber.org
Joe Galaxy	joegalaxy.net
MmChat	www.erols.com/clintg
MSN Messenger	messenger.msn.com
NetPopUp	www.vtoy.fi/~malo/netpopup.html
Odigo	www.odigo.com
Palace: Visual Chat	www.thepalace.com
Paltalk	www.paltalk.com

<u>Name:</u>	<u>Available On The Web At:</u>
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Peerchat	www.peerchat.com
Peopelink	www.peopelink.com
Pink Notes Plus	www.pinknotesplus.com
PowWow	www.tribal.com
QuickFlash	www.arm-group.com
ScreenFire	www.screenfire.com
Shizzam	home.xnet.com/~soliday1/shizzam
TalkR	www.acacia-net.com/romain/talkr.htm
WorldChat	home.sunrise.ch/compag/sds/wchatfw.html
Vypress Messenger	www.vypress.com
Yahoo! Messenger	messenger.yahoo.com

Most of these IM services are free to use, so consumers can choose the program or programs that best meet their needs. As a practical matter, then, even without interoperability, Internet users today can exchange instant messages, regardless of their preferred IM provider. AOL distributes its AIM software for free, as do a significant number of other IM providers, including many of those listed above. Internet users including subscribers to the AOL online service are able to use more than one IM client simultaneously. As a result, an Internet user, with little effort, can exchange instant messages with virtually any other Internet user, simply by downloading and installing the IM software used by the intended recipient.

c. If not, how is this beneficial to AOL and its IM customers?

AOL is involved, as demonstrated by its recent submission to the IETF, in efforts to develop an interoperability standard that will allow IM users to exchange instant messages regardless of their chosen IM service and in a way that does not jeopardize user privacy and security or the integrity of AOL's network. Until such an open standard is adopted, however, AOL will continue to regard the privacy and security interests of its users as its top priorities. As a result, AOL members and AIM users will benefit in two ways. First, while work continues on a suitable IM interoperability standard, our instant message users will continue to enjoy the privacy and security protections currently offered by our service. Second, once a standard that incorporates these safeguards is adopted, AOL members and AIM users and, indeed, all IM users will be able to exchange instant messages across IM services in an environment that is specifically designed to ensure that their passwords and personal information are secure, and that protects them from unsolicited instant messages.

AOL believes that protecting the privacy and security of its AOL members and AIM users should be its highest priority. AOL is proud of its efforts to safeguard the interests of instant messaging users both within the AOL service and through AIM, which include:

- Privacy Controls** allowing users to block other people from seeing if they are online or sending them messages;
- Knock-Knock** a pop-up box that gives AOL members and AIM users the option of whether or not to open a message sent by a stranger;
- Neighborhood Watch** a feedback option that allows AOL members and AIM users to identify improper behavior or violations of the Terms of Service;
- Anti-Spam Technologies** designed to prevent AOL members and AIM users from being deluged with thousands of unwanted messages including a limit on the number of messages that can be sent from one account; and
- AOL s Privacy Policy** a clear and easily obtainable policy outlining exactly what information AOL collects and what choices AOL members and AIM users can make about its use.

Competing IM providers have sought to allow their users to exchange instant messages with AOL members and AIM users either through unauthorized attempts to hack into AOL s IM servers or by advocating proposals that fail to address many of the technical, security, and privacy-related issues surrounding IM interoperability. Such proposals would sacrifice the user privacy and security that AOL has worked to protect. In short, we believe that any approach which would require consumers to register for accounts with every instant messaging system they use and force them to manage multiple IDs and passwords is seriously flawed and will not result in convenient, secure, or truly open interoperability. More importantly, forcing consumers to disclose their passwords whenever they send messages across systems would make them increasingly susceptible to hackers.

The better approach and the one advanced by the proposed architectural design for a worldwide IM system AOL submitted to the IETF is to first resolve the technical, security, and privacy-related challenges of building a secure and open system. Indeed, had the industry been more deliberate in the development of e-mail protocols, many of the issues that consumers encounter today with respect to e-mail including offensive spam and viruses might have been avoided.

- d. If so, are the alternate IM providers required to sign a licensing agreement that includes payment to AOL for access to AOL customers?**

AOL has not required payment for the licensing of its IM technology.

- e. Does AOL pay for access to alternative IM providers customers?**

As noted above, AOL does not demand payment in exchange for use of its IM technology. Likewise, AOL does not pay for access to other providers customers.

Ms. Royce Dickens
June 26, 2000
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1.14 Please provide copies of the 1999 annual reports and SEC 10-K filings for AOL and Time Warner.

As noted above, the parties are providing documents in response to this request under separate cover letter.

* * *

In conjunction with the documents the parties will be providing under separate cover letter, this completes AOL and Time Warner's response to the requests made in the June 9, 2000 letter from Ms. Truong. Please do not hesitate to contact the undersigned should you have any questions regarding this letter or the documents produced herewith.

Respectfully submitted,

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